No. 77-1413

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

JANE ARONSON, *Petitioner,*

v.

QUICK POINT PENCIL COMPANY, *Respondent.*

On Writ of Certiorari to the United States Court of Appeals For the Eighth Circuit

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BRIEF FOR THE RESPONDENT

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OPINIONS BELOW

The findings of fact and conclusions of law of the United States District Court for the Eastern District of Missouri (App. 60-64) are reported at 425 F. Supp. 600 (E.D. Mo. 1976). The opinion of the Eighth Circuit Court of Appeals (App. 66-83) is reported at 567 F.2d 757.

JURISDICTION

The judgment of the Court of Appeals for the Eighth Circuit was entered December 8, 1977. (App. 84.) A petition for rehearing was denied January 4, 1978. (App. 85.) The petition for a writ of certiorari was filed April 4, 1978, and was granted June 5, 1978. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

1. Whether a licensing contract made with respect to a specific patent application, which requires the licensee to continue paying royalties indefinitely despite the fact that the patent application was later abandoned, is invalid because it conflicts with the objectives of the United States patent laws.

2. Whether a contract requiring a patent application licensee to continue paying royalties indefinitely on the subject matter of an abandoned patent application, which is not a trade secret and which is being freely produced by the licensee's competitors, conflicts with national competition policy and decisions of this Court requiring full and free competition in the use of ideas in the public domain.

3. Whether a contract requiring a patent application licensee to continue paying royalties indefinitely on the subject matter of an abandoned patent application, which conflicts with both national competition policy in general and the United States patent laws in particular, is preempted by federal law and policy.

4. Whether the contract, in light of all the circumstances, should be construed to require payment of royalties after the patent application is abandoned.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Constitution of the United States:

Article I, Section 8, clause 8.

> The Congress shall have Power . . .
>
> To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries . . . .

Article VI, clause 2.

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land; . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Statutes:

35 U.S.C. § 101.

> Whoever invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefor, subject to the conditions and requirements of this title.

35 U.S.C. § 102.

> A person shall be entitled to a patent unless—. . .
>
> (b) the invention was . . . in public use . . . in this country, more than one year prior to the date of the application for patent in the United States . . . .

35 U.S.C. § 103.

> A patent may not be obtained though the invention is not identically disclosed or described as set forth in section 102 of this title, if the differences between the subject matter sought to be patented and the prior art are such that the subject matter as a whole would have been obvious at the time the invention was made to a person having ordinary skill in the art to

which said subject matter pertains. Patentability shall not be negatived by the manner in which the invention was made.

35 U.S.C. § 133.

Upon failure of the applicant to prosecute the application within six months after any action therein, of which notice has been given or mailed to the applicant, or within such shorter time, not less than thirty days, as fixed by the Commissioner in such action, the application shall be regarded as abandoned by the parties thereto, unless it be shown to the satisfaction of the Commissioner that such delay was unavoidable.

35 U.S.C. § 154.

Every patent shall contain a short title of the invention and a grant to the patentee, his heirs or assigns, for the term of seventeen years, subject to the payment of issue fees as provided for in this title, of the right to exclude others from making, using or selling the invention throughout the United States, referring to the specification for the particulars thereof. A copy of the specification and drawings shall be annexed to the patent and be a part thereof.

35 U.S.C. § 261.

Subject to the provisions of this title, patents shall have the attributes of personal property.

Applications for patent, patents, or any interest therein, shall be assignable in law by an instrument in writing. The applicant, patentee, or his assigns or legal representatives may in like manner grant and convey an exclusive right under his application for patent, or patents, to the whole or any specified part of the United States.

35 U.S.C. § 271.

(a) Except as otherwise provided in this title, whoever without authority makes, uses or sells any patented invention, within the United States during the term of the patent therefor, infringes the patent.

STATEMENT

This case involves an exclusive licensing agreement under which the petitioner Jane Aronson (formerly Jane Leopoldi) gave the respondent Quick Point Pencil Company ("Quick Point"), a small Missouri corporation which manufactures specialty products for the advertising industry, the "exclusive right" to manufacture and sell a keyholder upon which she had a pending patent application. (App. 18.) In this action, petitioner contends that Quick Point must pay royalties on the keyholder *indefinitely* even though the patent which both parties assumed would issue has never been granted, the patent application has been abandoned, and Quick Point has never received the "exclusive right" for which it bargained.

On October 25, 1955, petitioner filed with the United States Patent Office a Patent Application, Serial No. 542677, on a simple keyholder consisting of a wire clip which fastens around a small plastic disc. (App. 4.)

In June, 1956, petitioner, accompanied by her agent and then husband, Norbert Leopoldi, went to Quick Point's offices in St. Louis, Missouri, to negotiate a licensing contract for the keyholder covered by petitioner's patent application. (App. 17.)

In a letter to petitioner dated June 26, 1956, Quick Point, through its President, G.A. Goessling (now deceased), set forth its proposed licensing agreement. (App. 23-24.) This contract, which was subsequently accepted by petitioner (App. 24), explicitly stated that Quick Point would have the "exclusive right to make and sell keyholders of the type shown in your application, Serial No. 542677." (App. 23.) For this "exclusive right," Quick Point agreed to pay a 5% royalty on all keyholders described in the patent application that it sold. (App. 23.) In addition, the contract specified what action Quick Point would take in "the event of any infringement." (App. 24.) Since the agreement was "to make and sell," it contained no provisions concerning confidentiality or restricting disclosure of the keyholder design. (App. 23-25.)

Petitioner received the Quick Point letter on June 27, 1956, and telephoned Mr. Goessling the same day. Petitioner then drafted, on the letterhead of "N. Leopoldi," two additional paragraphs as an addendum to Mr. Goessling's proposed exclusive licensing agreement. (App. 25.) The first of these paragraphs provided that:

> In the event that the Keyholder Patent Application number 542677 is not allowed within five (5) years, Quick Point Pencil Co. agrees to pay Jane Leopoldi two and one-half percent ($2\frac{1}{2}\%$) of sales, at selling prices, as long as you continue to sell same.

Petitioner signed the licensing agreement and her own addendum on June 27, 1956, and forwarded these papers to Mr. Goessling in St. Louis. (App. 17.) Mr. Goessling signed the addendum in St. Louis and returned it to petitioner as an enclosure to a letter dated July 13, 1956. (App. 17.)

In July, 1956, Quick Point began manufacturing the keyholder covered by petitioner's Patent Application No. 542677, paying petitioner a 5% royalty on gross sales. (App. 18.) On June 26, 1961, five years after the date of the license, petitioner's royalty was reduced to $2\frac{1}{2}\%$ of sales, pursuant to the addendum, because petitioner had not been granted a patent on the application within five years. (App. 18.)

The patent, upon which the parties' exclusive licensing agreement was predicated, has never been granted. In 1956, the U.S. Patent Office rejected petitioner's Patent Application No. 542677. Petitioner filed an amendment to her original application, but the Patent Office in 1957 also rejected this amended application. The Patent Office Board of Appeals rejected petitioner's appeal of the rejection of her patent application on September 27, 1961, and petitioner thereafter abandoned her application. (App. 20.)[1]

As petitioner acknowledges (Br. 4), her keyholder could be readily copied by others as soon as it was marketed: that is, the keyholder could be literally "copied"; there is no question of "reverse engineering." By the

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[1] On April 4, 1961 (some five months before petitioner abandoned her patent application), petitioner's agent and former husband, Norbert Leopoldi, filed a patent application, Serial No. 104496, covering a similar keyholder device. (App. 18.) Mr. Leopoldi obtained a patent on his keyholder in 1964. (App. 18-19.) It was with respect to this keyholder that Quick Point's outside counsel wrote to Mr. Leopoldi, discussing Quick Point's obligations under the contract with petitioner and informing him that the Aronson-Quick Point agreement prevented him from licensing his keyholder to anyone other than Quick Point. (App. 39.)

late 1960's, keyholders substantially identical to that exclusively licensed by petitioner to Quick Point began appearing on the market. (App. 20.) Quick Point's competitors do not pay royalties on the keyholders they sell. (App. 57.) The royalty payments to petitioner add to Quick Point's cost, thereby making it difficult for Quick Point to compete effectively in the keyholder market (App. 21), and Quick Point's share of the keyholder market, not surprisingly, has been continually eroding (App. 57), although its aggregate sales have increased.

From the date of the licensing agreement through September 30, 1975, Quick Point has paid petitioner royalties of $203,963.84. (App. 19.) As of October 1, 1975, Quick Point, on the advice of counsel, ceased making royalty payments to petitioner. (App. 22.)

On November 18, 1975, Quick Point filed an action in the Eastern District of Missouri, based on diversity of citizenship, seeking a declaratory judgment. (App. 3-11.) Quick Point sought to have its licensing agreement with petitioner declared unenforceable with regard to future royalty payments on the ground that a licensing agreement which provides for payment of royalties indefinitely on an article for which a patent was applied but never granted conflicts with the Supremacy Clause and Article I, Section 8, clause 8 of the United States Constitution. (App. 5.)

The district court took the case under submission on a record consisting of a joint stipulation of uncontested facts and affidavits filed in support of cross-motions for summary judgment. (App. 61.) The district court concluded that federal patent principles were not relevant and ordered Quick Point to continue paying royalties to petitioner as long as Quick Point continued to manufacture the keyholder. (App. 60.)

Quick Point appealed to the United States Court of Appeals for the Eighth Circuit (App. 65), contending (1) that the district court had erred in holding that the case was governed solely by state contract law (App. 68), and (2) that there was no continuing liability under the contract, as a matter of contract law, when the patent was not issued. *See* Appellant's Br. below, pp. 25-29. The Eighth Circuit Court of Appeals agreed. The court noted that in the licensing agreement petitioner had promised Quick Point the "exclusive right" to manufacture her keyholder, and stated the issue to be (App. 68):

> whether Quick Point, a patent application licensee, is bound by the contractual provision requiring it to pay royalties for as long as it manufactures the item described in the patent application even though the licensor abandoned the application many years ago and the licensee's competitors are freely manufacturing the unpatented item.

The Eighth Circuit concluded that Quick Point, which had contracted for the exclusive right to manufacture and sell an item covered by a patent application, could not be forced to continue paying royalties on the item where the licensor had abandoned the patent application and had never obtained the patent which formed the explicit basis of the agreement. (App. 73.) The court reasoned that forcing Quick Point to continue paying royalties under these circumstances would conflict with federal patent law and policy. (App. 73.) Accordingly, it reversed the judgment of the district court. On June 5, 1978, this Court granted the petition for a writ of certiorari.

SUMMARY OF ARGUMENT

Petitioner entered an exclusive licensing agreement with respondent Quick Point Pencil Company ("Quick Point"), with respect to a pending patent application for a keyholder that petitioner had developed. Under this agreement, petitioner was to provide Quick Point the "exclusive right" to manufacture and sell the keyholder. As petitioner admits, exclusivity may be obtained only by obtaining a patent (Br. 19), but the patent on which this agreement was based never issued, and several companies now are manufacturing the keyholder that petitioner had promised Quick Point it would have the "exclusive right to make and sell."

Petitioner, nevertheless, takes the position that Quick Point is obligated to continue paying royalties on the sale of the keyholder even though the patent on which the contract was founded never issued, the patent application was abandoned, and respondent never received the "exclusive right" for which it had bargained. The Court of Appeals for the Eighth Circuit correctly found that forcing Quick Point to pay royalties under these circumstances would conflict with federal patent law and policy.

1. This case does not involve a trade secret or know-how licensing agreement; it involves a licensing agreement with respect to a specific patent application. The keyholder does not qualify as a trade secret because it does not meet the criteria of use in business, production of a competitive advantage, or even secrecy. Restatement of Torts, § 757, comment b, at 5, 6 (1939). Petitioner did not use the keyholder in her business, nor did it lend her a competitive advantage. Once marketed, the petitioner's idea was disclosed to all the world and could be readily copied, as petitioner concedes. (Br. 4.) Thus, this case is readily distinguishable from *Kewanee Oil Co.* v. *Bicron Corp.,* 416 U.S. 470, in that no trade secret is involved. Similarly, the licensing agreement does not involve know-how licensing. No body of technology or package of material was involved. Rather, the agreement was made with respect to a pending patent application for a single item, and, unlike the typical "know-how" agreement, not for a package of business skills. Having contracted to convey to respondent the "exclusive right" to manufacture and sell the keyholder in return for royalty payments, and having no trade secret or "know-how" to convey, the conclusion is inescapable that the contract was with respect to a pending patent application. Otherwise, petitioner could convey no exclusive right, for as the Court has repeatedly noted, *see, e.g., Gayler* v. *Wilder,* 10 Howard 477, 492-93, the right to exclusive exploitation of an invention is conferred only by the patent laws.

Thus, the issue before the Court is, as the Eighth Circuit correctly recognized, the obligation of a patent application licensee to continue paying royalties indefinitely on the subject matter of the patent application after the patent application has been abandoned and the subject matter of it is being freely manufactured and sold by the licensee's competitors.

2. A contract that requires a patent application licensee to continue paying royalties indefinitely on the subject matter of an abandoned patent application conflicts with the objectives of the federal patent laws and is, therefore, unenforceable. Enforcement of the contract provision at issue in this case would create incentives to avoid use of the federal patent system

which, in turn, would undermine the policy of the patent laws to encourage disclosure of new inventions. If the licensing agreement at issue here were upheld, inventors would be encouraged to use the leverage afforded by their pending patent applications to obtain highly favorable licensing agreements providing for royalties extending far into the future and then to abandon the applications upon which their agreements were based. This is because an inventor, such as the petitioner in this case, could collect royalties for only seventeen years if he obtained a patent on his invention, *Brulotte* v. *Thys Co.,* 379 U.S. 29, 33; however, if he abandoned his application, he could collect royalties forever. The incentive to apply for and abandon a patent is further enhanced by the fact that if a patent were to issue, and later be declared invalid, the licensee would no longer be obligated for most past royalties due. *Lear, Inc.* v. *Adkins,* 393 U.S. 653, 672-73, but if a patent were applied for and abandoned, the licensee would continue to be obligated for all past and future royalties. There would be no parity between an inventor to whom a patent issued and one who had applied for a patent but later abandoned the application. Thus, this contract cannot be enforced because it would discourage recourse to the federal patent system, *Kewanee Oil Co.* v. *Bicron Corp.,* 416 U.S. 470, and allow states to extend "perpetual protection to articles too lacking in novelty to merit any patent at all under federal constitutional standards. This would be too great an encroachment on the federal patent system to be tolerated." *Sears, Roebuck & Co.* v. *Stiffel Co.,* 376 U.S. 225, 232.

3. Requiring a patent application licensee to continue paying royalties on the subject matter of an aban-

doned patent application where the subject matter of the application is being freely produced by the licensee's competitors would undercut "the strong federal policy favoring the full and free use of ideas in the public domain," long followed by this Court. *Lear, Inc.* v. *Adkins,* 395 U.S. 653, 674; *see Kewanee Oil Co.* v. *Bicron Corp.,* 416 U.S. 470; *Goldstein* v. *California,* 412 U.S. 546; *Sears, Roebuck & Co.* v. *Stiffel Co.,* 376 U.S. 225; *Compco Corp.* v. *Day-Brite Lighting, Inc.,* 376 U.S. 234. Petitioner's keyholder is an idea in the public domain and requiring continued royalty payments on it would require the public "continually . . . to pay tribute to would-be monopolists without need or justification." *Lear, Inc.* v. *Adkins,* 395 U.S. 653, 670. Such forced tribute, required under the guise of state law, is anti-competitive and contrary to the principles enunciated by this Court in the cases cited above.

4. This contract, because it conflicts with both national competition policy in general and the United States patent laws in particular, is preempted by federal law. *Lear, Inc.* v. *Adkins,* 395 U.S. 653.

5. The contract should not be construed to require royalty payments to be continued indefinitely. Petitioner explicitly promised respondent the "exclusive right" to manufacture and sell her keyholder and agreed that in the event of "infringement" both parties would agree what action would be taken. Because petitioner abandoned her patent application, she never received the right to sue for infringement and respondent never received the "exclusive right" to manufacture and sell petitioner's keyholder. This failure of consideration discharges respondent's duty to provide further royalty payments to petitioner. Restatement of Contracts § 288 (1932); *see Drackett Chemical Co.* v. *Chamberlain Co.,* 63 F.2d 853 (6th Cir. 1933).

ARGUMENT

I. THIS CASE INVOLVES ONLY A LICENSING AGREEMENT MADE WITH RESPECT TO A SPECIFIC PATENT APPLICATION; IT DOES NOT AFFECT OR OTHERWISE INVOLVE THE ENFORCEABILITY OF TRADE SECRET OR KNOW-HOW LICENSING AGREEMENTS.

It is important at first to state the narrow issue that is actually before the Court.

The decision of the court below involves an agreement made specifically with respect to a pending patent application. The Eighth Circuit held that respondent could not be forced to continue paying royalties indefinitely for the manufacture and sale of the item which was described in the patent application when the application had been abandoned seventeen years ago, and the article to which it related was being freely manufactured and sold by respondent's competitors.[2]

Petitioner and amici curiae have taken a much broader view of the issues presented for decision by this Court than is warranted by the limited scope of the decision below and the specific facts presented in this case. Influenced by this expansive reading of the

[2] In the first four points of this Brief, it is assumed, for purposes of the argument, that the contract between the parties properly construed does call for the payment of royalties for an indefinite, perpetual period. Even on that construction of the contract, the respondent contends, for the reasons set forth below, that its obligation to pay royalties has terminated, as a matter of law. In the final point of this Brief, it is contended that, in the light of all the circumstances of this case, the agreement between the parties should not be construed as requiring royalty payments after the patent application was abandoned. By that time, it was clear that a substantial part of petitioner's promise to the respondent, that is, the "exclusive right" to produce the keyholder, was no longer forthcoming from the petitioner.

decision below, petitioner (and amici) assert that the decision casts doubt on all types of licensing agreements, including licenses of trade secrets and other know-how. (Br. 33.) This assertion confuses the holding below with other questions which are not at issue here. This case involves neither trade secrets nor know-how licensing agreements.

A. Petitioner's Simple Keyholder Device Is Not a Trade Secret.

Contrary to the dissenting opinion below (App. 73-83), this case does not involve a trade secret. Petitioner's design for a keyholder never amounted to a trade secret for it lacked the two unique characteristics which distinguish trade secrets from other types of intellectual property and which provide the economic and public policy justification for their protection.

A trade secret must be used continuously in the owner's business and lend him a competitive advantage. Restatement of Torts, § 757, comment b, at 5 (1939).[3]

[3] The Restatement of Torts, § 757, comment b, at 5 (1939), defines a trade secret as follows:

> A trade secret may consist of any formula, pattern, device, or compilation of information *which is used in one's business, and which gives him* [*the owner*] *an opportunity to obtain an advantage over competitors who do not know or use it.* It may be a formula for a chemical compound, a process of manufacturing, treating or preserving materials, a pattern for a machine or other device, or a list of customers. It differs from other secret information in a business (see § 759) in that it is not simply information as to single or ephemeral events in the conduct of the business, as, for example, the amount or other terms of a secret bid for a contract or the salary of certain employees, or the security investments made or contemplated, or the date fixed for the announcement of a new policy or for bringing out a new model or the like. *A trade secret is a process or device for continuous use in the operation of the business.* . . . (Emphasis added.)

Businesses normally devote substantial resources and time to developing secret manufacturing processes and similar business materials having *competitive* value. As this Court noted in *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 485, if such property were not afforded protection from unauthorized use and disclosure, businesses might lose the incentive to invest in the development of new processes and materials. Alternatively, businesses would be forced to rely on self-help measures to keep their secret processes to themselves, thereby diverting valuable economic resources from productive to protective uses. *Kewanee Oil Co.* v. *Bicron Corp., supra,* 416 U.S. at 485-86.

These policy considerations do not apply here because petitioner's simple keyholder, unlike the secret industrial process this Court considered in *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470,[4] fails to meet this

[4] In the *Kewanee Oil* case, this Court held that trade secret law is not preempted by federal patent law. *Kewanee Oil* is a classic trade secret case which bears no factual similarity to this case.

In *Kewanee Oil*, employees misappropriated a secret process for the growth of synthetic crystals, which was developed and used in the course of their employer's business. 416 U.S. at 473. The secret process could not be readily ascertained by the employer's competitors when the product was marketed. Indeed, the secret process had not been discovered at the time of trial. 416 U.S. at 473-74. This Court, emphasizing the state's strong interest in preventing "industrial espionage" and similar breaches of confidentiality, 416 U.S. at 487, held that the district court had properly applied the state trade secret law by enjoining the employees' disclosure or use of certain of their employer's trade secrets until such time as the trade secrets had been released to the public, had otherwise become generally available, or had been obtained from sources having the legal right to convey the information. 416 U.S. at 473-74. Unlike *Kewanee Oil*, the present case involves neither misappropriation nor a *bona fide* trade secret.

basic prerequisite of trade secret protection. Petitioner is an aspiring inventor who sought a patent, and obtained a licensing agreement with respect to her pending patent application. Petitioner at no time "used" the keyholder in her "business," whether continuously or otherwise, and the keyholder lent her no competitive advantage. Where these criteria are not met, an invention—no matter what its other attributes may be —cannot qualify as a trade secret. 2 Milgrim, *Trade Secrets* § 8.03, at 8-35 to 8-37 (1978).

Further, petitioner's simple keyholder device does not qualify as a "secret." The respondent's licensing agreement gave it the right to "make and sell" the product (App. 23), and the mere fact of putting it on the market, pursuant to the contract, fully disclosed the idea to the whole world. From that time forward, the only protection was in the patent application. There was no secret process. There was nothing to be held confidential. From the moment of the first authorized sale, there was no secret.

To qualify for trade secret protection "a substantial element of secrecy must exist, so that, except by the use of improper means, there would be difficulty in acquiring the information." Restatement of Torts, § 757, comment b, at 6 (1939). Consequently, matters which are completely disclosed upon marketing cannot be trade secrets. *Id.* A device readily ascertainable by members of the trade, as is petitioner's keyholder (App. 20-21), cannot be a trade secret, for while "[a trade] secret need not be novel or inventive in a patentable sense, it must 'possess at least that modicum of originality which will separate it from everyday knowledge' and must be more than 'ordinary mechanical commonality.'" *Keystone Plastics, Inc.* v. *C & P Plas-*

tics, Inc., 340 F. Supp. 55, 74 (S.D. Fla. 1972), *quoting Cataphote Corp.* v. *Hudson*, 444 F.2d 1313, 1315 (5th Cir. 1971), *aff'd*, 506 F.2d 960 (5th Cir. 1975).[5] Lacking the essential attribute of secrecy, petitioner's keyholder was not a trade secret nor entitled to protection as a trade secret. As the Eighth Circuit correctly recognized (App. 68), petitioner, unlike the Kewanee Oil Company in *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, is not—and never has been—a trade secret owner.

B. Petitioner's Simple Keyholder Device and the Licensing Agreement Here Are Clearly Distinguishable From Confidential Disclosures of Packaged Business Know-How.

Know-how, although not susceptible to precise definition,[6] may be considered a body of technology, ordinarily unpatented and unpatentable, which is useful in making a product for commercial sale. Worthing, *Know-How Misuse: A Potential Weapon for Licensees*, 53 J. Pat. Off. Soc'y 177, 178 (1971).[7] A know-how license may include such items as engineering drawings, fixtures, bills of material and even the brainpower of the licensor's personnel. *Id.* Although it may, as amicus The American Patent Law Association notes, contain some patented articles (Br. 22, A-1), the *body* of materials conveyed pursuant to a know-how licensing agreement is clearly unpatentable and the parties to such an agreement do not contract with specific reference to the patentability of any given article within the package.

As amicus The American Patent Law Association itself acknowledges, such packaged business know-how is readily distinguishable from petitioner's simple keyholder device. (Br. 22.) Unlike the typical know-how license, petitioner and Quick Point in this case contracted with regard to only one item which clearly falls within the category of subject matter patentable under 35 U.S.C. § 101 (1970). Unlike a typical know-how license, Quick Point and petitioner contracted with specific reference to a pending patent application on that one item, and considered the granting of a patent on the device to be of basic importance. Thus, the subject matter of this case bears no resemblance to the type of packaged business know-how and "what-not-to-use" information described for this Court at considerable length by The American Patent Law Association.

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[5] Similarly, in *Sarkes Tarzian, Inc.* v. *Audio Devices, Inc.*, 166 F. Supp. 250 (S.D. Cal. 1958), *aff'd per curiam*, 283 F.2d 695 (9th Cir. 1960), *cert. denied*, 365 U.S. 869, the court stated that a trade secret "must consist of a particular form of construction of a device, a formula, method or process that is of a character which does not occur to persons in the trade with knowledge of the state of the art or which cannot be evolved by those skilled in the art from the theoretical description of the process, or compilation or compendia of information or knowledge." *Id.* at 257-58. *See also Wilkin* v. *Sunbeam Corp.*, 377 F.2d 344, 347 (10th Cir. 1967), *cert. denied*, 389 U.S. 973 (no trade secret where principles incorporated in appellant's device were known to industry prior to appellant's application for patent); *American Gage & Mfg. Co.* v. *Maasdam*, 245 F.2d 62, 64 (6th Cir. 1957) (no trade secrets or know-how imparted; device completely disclosed elements of construction).

[6] One commentator has stated that know-how is "an amorphous, ill-defined glob of technology that has no clear time limits and no clear geographical limits. Its subject matter is not only vaguely defined; it is not even publicly defined." Stedman, *Legal Problems in the International and Domestic Licensing of Know-How*, 29 A.B.A. Sec. Antitrust Law 247, 250 (1965).

[7] Similarly, amicus curiae The Patent, Trademark and Copyright Section of the State Bar of Texas defines know-how as "the specialized knowledge of how to economically and effectively perform a given task" and notes that such information is seldom patentable. (Br. 10.)

C. Petitioner's Agreement With Quick Point Is a License Under a Pending Patent Application Pursuant to Which Quick Point Agreed to Pay Royalties for the "Exclusive Right" to Manufacture and Sell Petitioner's Keyholder Device.

Petitioner and amici curiae erroneously equate the royalty agreement at issue in this case to a typical trade secret or know-how license in which the licensee bargains only for disclosure. *See infra* at 22. This characterization directly contradicts the conclusion reached by the court below (App. 68),[8] and completely ignores

[8] The dissent below also erroneously concluded that the agreement at issue in this case is a trade secret license. (App. 74.) The majority, however, noted that "[t]he agreement was not for disclosure but for the exclusive right to manufacture an invention that was to be patented" (App. 69), and explicitly characterized the respondent as a patent application licensee. (App. 68.)

Nevertheless, the United States contends that "[t]he court's decision rests entirely on the proposition that federal law prevents enforcement of valid trade secret licenses" (Br. 9, at n. 2), claims that the character of the parties' agreement makes little difference to the outcome of this case (Br. 9), and suggests that the agreement may be understood as either a trade secret license or as a promise to pay petitioner for services rendered in designing the keyholder. (*Id.*)

Both of these characterizations by amicus United States of the agreement at issue in this case are incorrect. Petitioner's keyholder is not and has never been a trade secret (*see supra* at 15-18) and Quick Point contracted not for petitioner's services but rather for the "exclusive right to make and sell" petitioner's product (*see infra* at 21). Furthermore, the fact that this agreement was under a pending patent application is both central to the decision below and of crucial importance to the disposition of this case. By refusing to identify and come to terms with the particular type of licensing agreement at issue in this case, the United States further beclouds the issue before this Court and advances legal arguments which are erroneously keyed to trade secret licenses in general rather than to the specific type of patent application licensing agreement at issue in this case.

the plain language of the licensing agreement, which states that Quick Point was to obtain the "exclusive right to make and sell" the keyholder which was the subject of petitioner's pending patent application in consideration for a 5% royalty on all keyholders of that type it sold.[9]

The right to exclusive exploitation of an invention is one granted only by the patent laws and only a patentee can convey this exclusive right. *See, e.g., Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 490; *Marsh* v. *Nichols, Shepard & Co.*, 128 U.S. 605, 612; *Gayler* v. *Wilder*, 10 Howard 476, 492-93.[10] In contrast to a pat-

[9] The agreement states, *inter alia*, that (App. 7):

> Quick Point Pencil Company will have the *exclusive right to make and sell* keyholders of the type shown in your application, Serial No. 542677, and will start manufacturing within 60 days after you indicate your acceptance of the following terms.
>
> We will pay you $750.00 right away as an advance payment on royalties; the royalty rate will be 5% of our selling price (not to include shipping charges) on all keyholders which we make in accordance with the design shown in your application, Serial No. 542677.
>
> * * *
>
> *In the event of any infringement*, as I discussed with Mr. Leopoldi, we will at the time decide between us any action that should be taken. However, we will not agree to enter into litigation until a mutual conference and understanding can be reached between us. (Emphasis added.)

[10] The Sixth Circuit, quoting in part *Gayler* v. *Wilder*, *supra*, explained this principle as follows:

> The inventor of a new and useful improvement has no exclusive right to it until he obtains a patent. This right is created by the patent, but the discoverer is vested by law with an inchoate right to its exclusive use which he may perfect and make absolute by proceeding in the manner which the law requires and after an inventor files his application pursuant to the statute he may transfer all of this right by assignment or a part of it by license. *Baldwin Rubber Co.* v. *Paine & Williams Co.*, 107 F.2d 350, 353 (6th Cir. 1939).

ent licensor, neither a trade secret licensor nor the licensor of other know-how is able to guarantee exclusive use to a licensee because others are free to copy a trade secret or idea once it is disclosed or otherwise independently developed. *See, e.g., Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 490; *Painton & Co.* v. *Bourns, Inc.*, 442 F.2d 216, 223 (2d Cir. 1971). Consequently, the bargained-for consideration in a trade secret licensing agreement is disclosure, but the bargained-for consideration for a patent license is use in accordance with the license—in this case exclusive use.

> . . . [T]he license reward for a trade secret tends to be a function of consideration for disclosure; for a patent, consideration for use.
>
> * * *
>
> While trade secret and patent licenses are voluntary arrangements, there are important differences between them. In the former the parties do not contemplate public disclosure and the licensee knows that he has no protection against independent developers. In the latter, disclosure has occurred (or is about to occur) and the licensee relies upon the validity of the patent to protect against competitive use. Milgrim, *Sears to Lear to Painton: Of Whales and Other Matters*, 46 N.Y.U. L. Rev. 17, 30 (1971).

The licensing agreement in this case is neither a pure patent license, in which the *only* bargained-for consideration is exclusive use, nor a pure trade secret license, in which the *only* bargained-for consideration is disclosure. The contract petitioner negotiated with Quick Point is a licensing agreement under a pending patent application similar to the one this Court considered in *Lear, Inc.* v. *Adkins*, 395 U.S. 653, where the bargained-for consideration is a combination of dis-

closure and exclusive use. *See Lear, Inc.* v. *Adkins, supra,* at 682, n. 2 (White, J., concurring in part).

Like Lear, Quick Point bargained first for the disclosure of petitioner's idea and the immediate right to manufacture and sell petitioner's device during the time petitioner's patent application was pending, and secondly for the "exclusive right" to manufacture and sell the device once the contemplated patent was granted. *See Lear, Inc.* v. *Adkins, supra,* at 682, n. 2 (White, J., concurring in part).

As the Eighth Circuit correctly recognized (App. 68), petitioner's agreement with Quick Point is understandable only as a patent application license. The fact that Quick Point whether out of generosity [11] or because of outside counsel's misinterpretation of its rights and liabilities under the licensing agreement,[12]

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[11] Until the late 1960's, Quick Point continued to be the only manufacturer of petitioner's keyholder. During this period, Quick Point was, in fact, able to enjoy the "exclusive right" bargained for under its contract with petitioner, but this exclusivity resulted from chance marketplace conditions and not from any legal right to exclusivity bestowed by virtue of the contract with petitioner.

During the late 1960's, Quick Point's competitors began producing keyholders essentially the same as that which petitioner had failed to patent. (App. 20.) As Quick Point saw its market share continue to erode, it understandably felt more impelled to seek termination of its royalty payments than it had in earlier years when it faced no similar threat to its market position.

[12] Petitioner relies upon a letter written to Mr. Leopoldi by outside counsel (not an officer of respondent) with regard to a pending patent application filed by Mr. Leopoldi (not petitioner) as support for the proposition that Quick Point believed it was required to continue paying royalties to petitioner even though a patent on petitioner's invention never issued. (App. 20.) This reliance is misplaced. Counsel's opinion was his own, and it was erroneous. It was drafted five years after the original agreement and during

continued to pay royalties after 1961, when petitioner abandoned her application, in no way affects the character of the agreement as a license under a pending patent application.

D. The Issue Before This Court Is Narrowly Confined to the Question of Indefinite Royalty Payments Pursuant to Contracts Dealing With Patent Application Licenses.

This case does *not* concern a trade secret license such as that considered in *Warner-Lambert Pharmaceutical Co.* v. *John J. Reynolds, Inc.*, 178 F. Supp. 655 (S.D.N.Y. 1959), *aff'd per curiam*, 280 F.2d 197 (2d Cir. 1960).[13] Contrary to petitioner's assertions (Br. 33), this case does not concern licensing agreements for disclosure of non-copyrightable ideas such

the pendency of the patent application which both parties still thought would be granted, and which had to be granted if Quick Point was to have the "exclusive right" for which it had bargained. It is thus not reliable evidence of the parties' intent at the time they negotiated their licensing agreement. The second half of Quick Point's bargained-for consideration—exclusive use—failed to be realized when petitioner abandoned her patent application. This failure of consideration could, in and of itself, have discharged respondent's obligation to provide further royalty payments to petitioner. *See infra* at 48-53. When Quick Point was later correctly advised that it could cease paying royalties, it did so and immediately sought a declaratory judgment to that effect.

[13] Petitioner relies heavily on *Warner-Lambert* to support her position, but *Warner-Lambert* is readily distinguishable from this case. *Warner-Lambert* did not involve a patent, a patent application license, or a contract made with specific reference to a patent application. What it did involve was a trade secret which defendant's predecessors disclosed to plaintiff's predecessor in return for continuing royalty payments. Unlike the present case, the defendant there, as the trade secret owner, at no time filed a patent application on its discovery and its secret formula clearly constituted a *bona fide* trade secret.

as television formats. Contrary to petitioner's assertions (Br. 33) and its statement of the issues presented in this case (Br. 2), the decision below would not render unenforceable all licensing agreements for unpatented ideas which become public. Nor does the decision below render unenforceable or otherwise involve the type of complex, high technology packaged know-how licensing agreements which are the particular focus of the amicus curiae brief of The American Patent Law Association.

The decision below speaks only to the obligation of a *patent application licensee* to continue paying royalties indefinitely on the one item which is the subject of its license, long *after* the patent application upon which its licensing agreement was based was finally abandoned,[14] and the respondent's competitors are freely producing the item. It is this issue which the Eighth

[14] Petitioner has also incorrectly contended that the decision below renders unenforceable every license of a pending patent application. (Pet. for Cert. 17.) This specific issue was not even raised, much less decided, in the present action. From 1956 to 1961, when petitioner's patent application was pending, Quick Point paid all royalties due under the license. Quick Point has never contested these payments.

Although petitioner incorrectly contends further that the court below decided the question this Court left undecided in *Lear, Inc.* v. *Adkins*, 395 U.S. 653, there is nothing in the Eighth Circuit's opinion which concerns the enforceability of royalties *during the pendency of a patent application*, which is the specific issue this Court raised, but left undecided, in *Lear. Id.* at 674-75.

Quick Point does not seek any refund of the substantial royalties it has already paid to petitioner over a period of nineteen years. The only payments at issue in this case are *future continuing* payments to which petitioner, an unsuccessful patent applicant, claims she is entitled even though she could not as a *bona fide* patentee lawfully claim such payments. *See infra* at 28.

Circuit decided. It is this narrow issue which is before this Court.[15]

II. A CONTRACTUAL PROVISION REQUIRING A PATENT APPLICATION LICENSEE TO CONTINUE PAYING ROYALTIES INDEFINITELY ON THE SUBJECT MATTER OF AN ABANDONED PATENT APPLICATION CONFLICTS WITH THE OBJECTIVES OF THE PATENT LAWS OF THE UNITED STATES AND IS THEREFORE UNENFORCEABLE.

Article I, Section 8, clause 8 of the Constitution grants to Congress the power "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries. . . ."

Pursuant to this clause, Congress enacted the patent laws under which the inventor of a new, useful, and non-obvious invention may obtain a patent on his invention. 35 U.S.C. §§ 101-103, 154 (1970). In return for disclosure of his invention, the inventor obtains the right to exclude others from making, using, or selling his invention for seventeen years, 35 U.S.C. § 154 (1970), *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 477-78, and may assign this exclusive right to others to exploit in his stead, 35 U.S.C. § 261 (1970).

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[15] Amicus curiae, The Patent, Trademark and Copyright Section of the State Bar of Texas also urges this Court to consider only the narrow issue presented by the record and the decision below. (Br. 3, 15.) This is appropriate, for as shown above, the broad question petitioner urges this Court to decide was never considered, much less decided, by the court below and is not raised by this record. Yet as the briefs of the other amici curiae show, the broad question petitioner urges this Court to consider in the context of this narrow record involves complex questions of substantial economic and political importance for which a full record from the courts below is especially critical. Where such a record is lacking "sound principles . . . [dictate] that the Court not render a decision on questions unnecessary to the disposition of the case." *Lear, Inc.* v. *Adkins*, 395 U.S. 653, 678-79 (White, J., concurring in part).

This Court has firmly established that a state cannot, under the guise of any law, "give protection of a kind that clashes with the objectives of the federal patent laws." *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 231. Enforcement of petitioner's alleged contractual right to continue collecting royalty payments indefinitely on her unpatented device would not only undermine pro-competitive policy objectives consistently endorsed by this Court (*see infra* at 35-41), but would also conflict directly with the objectives of the federal patent laws.

A. Enforcement of the Contractual Provision in This Case Would Create Substantial Incentives to Avoid Recourse to the Patent System, Thereby Undermining the Preeminent Patent Law Objective of Encouraging the Disclosure of New Inventions.

The primary objective of the patent laws is to promote material and scientific progress by providing to inventors of patentable products monopoly rights for a limited period of time in return for disclosure of their patentable inventions. *See, e.g.*, *Scott Paper Co.* v. *Marcalus Manufacturing Co.*, 326 U.S. 249, 255. As this Court has repeatedly recognized, this disclosure requirement is at the heart of the patent system, for it is disclosure which stimulates ideas and the development of further significant advances in the art. *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 480-81.

The strong federal policy favoring disclosure of inventions is furthered by encouraging inventors to apply for and obtain patents on patentable inventions. As a result, any state law (or private contractual obligation enforced by state law) which causes a "substantial risk" that inventors of devices thought to be patentable would avoid seeking patent protection for their

inventions conflicts with the federal patent laws and cannot be enforced. *Kewanee Oil Co.* v. *Bicron Corp., supra,* 416 U.S. at 489.[16]

This risk is present in this case. If petitioner's position is accepted, inventors such as Aronson who believe their inventions to be patentable will have every incentive to license their inventions during the period their patent applications are pending, and then abandon their applications after they have obtained from their licensees favorable licensing agreements providing for royalty payments for periods of time in excess of those which are available to *bona fide* patentees.

A *bona fide* patentee may use the leverage of his patent to obtain royalties from a licensee for a maximum of seventeen years. *Brulotte* v. *Thys Co.,* 379 U.S. 29, 33.[17] Petitioner, however, urges this Court to find that she was entitled to use the leverage of her patent application to exact continuing royalties for an indefinite period of time despite the fact that she would not have been entitled to such royalties had she not aban-

[16] Petitioner agrees that any contractual provision which causes diversion from the patent system is unenforceable, but contends (citing only the dissenting opinion below) that there is no possibility of diversion in this case. (Br. 12-13.) This conclusion is shared by the dissent below (App. 81), and by the United States. (Br. 14.) Respondent here contends this is incorrect.

[17] *Brulotte* v. *Thys* is one of a long series of decisions in which this Court has established that state contract law may not create any exclusionary rights in the subject matter of expired patents. *See, e.g., Zenith Radio Corp.* v. *Hazeltine Research, Inc.,* 395 U.S. 100, 136-38; *Scott Paper Co.* v. *Marcalus Mfg. Co.,* 326 U.S. 249, 256-57; *Kellogg Co.* v. *National Biscuit Co.,* 305 U.S. 111, 119-20; *Singer Mfg. Co.* v. *June Mfg. Co.,* 163 U.S. 169, 185.

doned[18] her application and had instead secured a patent.

Unlike a typical trade secret agreement, in which the licensor never seeks patent protection but instead relies on trade secret protection as an *alternative* to the patent system, *see, e.g., Warner-Lambert Pharmaceutical Co.* v. *John J. Reynolds, Inc.,* 178 F. Supp. 655 (S.D.N.Y. 1959), *aff'd per curiam,* 280 F.2d 197 (2d Cir. 1960), petitioner in this case first filed a patent application, used this pending patent application as leverage to obtain a highly favorable licensing agreement providing for continuing royalty payments, and later abandoned the patent application which had given her this leverage.[19]

[18] Abandonment is defined as failure to prosecute a patent application within six months of action thereon by the Patent Office. 35 U.S.C. § 133 (1970); *see* 37 C.F.R. §§ 1.135-138 (1977).

[19] As Judge Friendly implicitly recognized in *Painton & Co.* v. *Bourns, Inc.,* 442 F.2d 216 (2d Cir. 1971), this situation must be carefully distinguished from the typical trade secret licensing situation in which a patent application is never filed. *Id.* at 225.

This is true, at least in part, because the rights of an inventor under a pending patent application have great prospective value. *Hobbs* v. *United States,* 376 F.2d 488, 493 (5th Cir. 1967); *Mullins Mfg. Co.* v. *Booth,* 125 F.2d 660, 664 (6th Cir. 1942).

In a typical trade secret licensing agreement, the licensee knows that his licensor is unable to guarantee him exclusive use of the article and makes his bargain accordingly. Milgrim, *Sears to Lear to Painton: Of Whales and Other Matters,* 46 N.Y.U. L. Rev. 17, 30 (1971); *see Dr. Miles Medical Co.* v. *John D. Park & Sons Co.,* 220 U.S. 373, 402. In contrast, where an inventor offers to license an article which is the subject of a pending patent application, the licensee also bargains for the future right to exclusive use of the invention for which the licensor can extract greater royalty payments than it could if the licensee were bargaining only for disclosure. *See Painton & Co.* v. *Bourns, Inc.,* 442 F.2d 216, 224 (2d Cir. 1971). This is especially true, where, as here, the licensed

From a business perspective, petitioner made a wise decision. Had the patent for which petitioner applied been granted in 1960 (*i.e.,* within five years), she would have been able to collect royalties at the rate of 5% only until 1977. Had the patent been granted in 1961 (the year Aronson finally abandoned her application), petitioner would have been able to collect royalties at a rate of 2½% only until 1978. Petitioner, having abandoned her application in 1961, now seeks to continue collecting royalties at the 2½% rate for an indefinite period of time, far in excess of the seventeen years to which she would have been entitled had she actually obtained a patent on her keyholder.

Petitioner, in effect, seeks rights as the holder of an abandoned patent application which exceed those of a

invention may be readily copied by competitors, and the right to disclosure is likely to be a short-lived benefit. Thus, although a licensee normally will not agree to pay as much for rights under a pending patent application as it would for a patent license, it will pay more for such rights than it will for mere disclosure under a trade secret license.

Furthermore, the presence of a pending patent application may exert an *in terrorem* effect on potential competitors and licensees. It may induce a manufacturing firm such as Quick Point to secure a license and pay royalties for a given product where it would not otherwise do so. This is because a pending patent application gives an inventor/licensor such as Aronson the power to go to one of the manufacturer's competitors and offer it the future exclusive right to manufacture its article if the first manufacturer does not meet its asking price. If the product offered is of sufficient value to the first manufacturer and it does not want to risk being foreclosed from producing the product in the future, it will be likely to accept the inventor/licensor's royalty terms rather than forego the future opportunity to compete.

Thus, contrary to the assumptions expressed in the dissenting opinion below (App. 81), the licensor is able to exert more leverage in negotiating royalties than is the licensee.

bona fide patentee. Although petitioner abandoned her application, she has already obtained from Quick Point royalties for nineteen years. If petitioner prevails in this action, she will be able to collect royalties indefinitely. "The result would be that while federal law grants only . . . 17 years' protection to genuine inventions . . . States could allow perpetual protection to articles too lacking in novelty to merit any patent at all under federal constitutional standards. This would be too great an encroachment on the federal patent system to be tolerated." *Sears, Roebuck & Co.* v. *Stiffel Co.,* 376 U.S. 225, 232.

This Court has held that the owner of a valid patent may not validly contract for payment of royalties beyond the patent period. *Brulotte* v. *Thys Co.,* 379 U.S. 29, 33. Moreover, where a patent is granted, a patent licensor runs a high risk of having his patent challenged and ultimately declared invalid.[20] If a patent is declared invalid, licensees may not only avoid paying future royalties, but they also may be relieved of the obligation to pay most past royalties due. *See Lear, Inc.* v. *Adkins,* 395 U.S. 653, 672-73.[21]

If a patent application licensor such as petitioner, after having obtained from its licensee a promise to

[20] "[M]ore than 80% of patent infringement actions on appeal result in a holding that the patent sued upon is invalid." Milgrim, *Sears to Lear to Painton: Of Whales and Other Matters,* 46 N.Y.U. L. Rev. 17, 31 (1971).

[21] As this Court noted in *Blonder-Tongue* v. *University Foundation,* 402 U.S. 313, "*Lear* permits an accused infringer to accept a license, pay royalties for a time, and cease paying when financially able to litigate validity, secure in the knowledge that invalidity may be urged when the patentee-licensor sues for unpaid royalties." *Id.* at 346.

continue paying royalties on the use of a given item indefinitely, could avoid the consequences of the *Lear* decision by later abandoning the patent application, the licensor would have everything to gain and nothing to lose by doing so.[22] Instead of wholeheartedly attempting to patent his invention, the licensor would have an incentive to exploit his invention through private contractual relationships enforced by the states. Consequently, "[p]rivate business would function as its own patent office and impose its own law upon its licensees. It would obtain by contract what letters patent alone may grant." *Mercoid Corp.* v. *Mid-Continent Investment Co.,* 320 U.S. 661, 667.

The contract for continuing royalties which petitioner seeks to enforce clearly creates a "substantial risk" of diverting inventions from the patent system. Consequently, this contract "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Hines* v. *Davidowitz,* 312 U.S. 52, 67, and is unenforceable under the principles

[22] Contrary to the assertions of the United States (Br. 14), the dual royalty provision did not give petitioner every incentive to prosecute her patent application. Petitioner would have collected a higher royalty if she had succeeded in obtaining a patent within five years. Consequently, until 1961, petitioner had some incentive to seek a patent on her device. After 1961, however, petitioner had no such incentive because, under her contention, she would collect 2½% in royalties thereafter whether or not she obtained a patent. At this point she would profit more by not actively continuing to seek a patent because she would, if she obtained a patent, be allowed to collect her 2½% in royalties for only seventeen years and subject herself to the further possibility of Quick Point challenging the patent. While none of the discussion above is meant to imply bad faith on the part of the petitioner, it is, nevertheless, true that, on her contention, petitioner, by 1961, had everything to gain and nothing to lose by abandoning further efforts to obtain a patent on her keyholder.

recently enunciated by this Court in *Kewanee Oil Co.* v. *Bicron Corp.,* 416 U.S. 470, 489.

B. Non-enforcement of This Licensing Agreement, Which, If Enforced, Would Require the Continued Payment of Royalties Far Into the Future, Would Not Discourage Invention.

Contrary to petitioner's contentions (Br. 13-15), non-enforcement of the licensing agreement at issue in this case would not discourage invention because this case does not concern the viability of either know-how licensing agreements or trade secret licenses in general. Quick Point does not contend that petitioner is entitled to no compensation for disclosing and licensing her invention. Nor does Quick Point contest petitioner's entitlement to substantial royalty payments. The question presented in this case is not *whether* a trade secret license may be enforced but rather *how long* a *patent application licensor* may continue to collect royalties on the subject matter of an abandoned patent application.[23]

[23] When seen from this perspective, the argument of both amicus and petitioner with regard to inducing lump sum payments (Pet. Br. 13, U.S. Br. 22-24) becomes irrelevant to the disposition of this case. If this Court holds that a patent application licensee can exact royalty payments for no longer than the seventeen-year period allowed to a *bona fide* patentee, the licensor could still exact royalties for a seventeen-year period. No short term or lump sum payments would be involved.

Alternatively, were this Court to hold that a patent application licensor could not collect any royalties after his application were abandoned, this would not necessarily induce lump sum, "up-front" payments. The licensor and licensee could still tie royalty payments to the actual sale of the product, and although the royalties might be negotiated at a higher rate than would be true for an agreement of longer duration, there is no more speculation required in setting royalty rates at an appropriate level in the latter case than in the former.

Quick Point already has paid royalties to petitioner for nineteen years. During the five-year pendency of petitioner's patent application, she collected approximately $27,000 in royalty payments from Quick Point. (App. 19.) Total royalty payments exceed $200,000. (App. 19.) The import of petitioner's arguments (*see* Br. 13-15), and those of amicus United States (Br. 11-13), is that such sums would not provide sufficient incentive for inventors to develop and market new products.

In effect, petitioner asks that this Court adopt the argument it rejected in *Lear, Inc.* v. *Adkins,* 395 U.S. 653. In *Lear,* the Court considered whether Adkins, an inventor, was entitled to collect royalties for the entire contractual period in return for pre-issuance disclosure of his invention to Lear. The Court decided he could not.

> The inventor does not merely argue that since Lear obtained privileged access to his ideas *before 1960,* the company should be required to pay royalties accruing *before 1960* regardless of the validity of the patent which ultimately issued. He also argues that since Lear obtained special benefits before 1960, it should also pay royalties during the entire patent period (1960-1977), without regard to the validity of the Patent Office's grant. We cannot accept so broad an argument. *Id.* at 672. (Emphasis in original.)

Petitioner, like Adkins, seeks to collect royalties not only for the period during which her application was pending but also for a period long after her idea had been rejected as unpatentable; she contends that if her agreement providing for *perpetual* royalties is not enforced, inventors will be discouraged from developing and marketing new products, thereby undermining innovation and the commercial exploitation of new ideas.

Quick Point does not question the need for encouraging such innovation; it does, however, submit that non-enforcement of *perpetual* royalty payments made with respect to a specific patent application for a period extending far beyond that to which petitioner would be entitled as a *bona fide* patent licensor, is neither required to encourage innovation nor allowable under the patent laws.

III. A CONTRACT REQUIRING A PATENT APPLICATION LICENSEE TO CONTINUE PAYING ROYALTIES INDEFINITELY ON THE SUBJECT MATTER OF AN ABANDONED PATENT APPLICATION, WHERE THE SUBJECT MATTER OF THE LICENSE IS NOT A TRADE SECRET AND IS BEING FREELY PRODUCED BY THE LICENSEE'S COMPETITORS, FRUSTRATES NATIONAL COMPETITION POLICY.

A. Federal Policy Requires Full and Free Competition in the Use of Ideas in the Public Domain.

The patent system, insofar as it confers monopoly powers, is a limited exception to the policy of free competition which lies at the heart of our economic and political system. *Precision Instrument Manufacturing Co.* v. *Automotive Maintenance Machinery Co.,* 324 U.S. 806, 816. Accordingly, this Court has recognized the exceptional position of the patent system within our economy and has prohibited any attempt to broaden the temporal or substantive scope of the patent monopoly. *Blonder-Tongue Laboratories, Inc.* v. *University Foundation,* 402 U.S. 313, 343.[24]

[24] *See, e.g., International Salt Co.* v. *United States,* 332 U.S. 392, 395-96; *Morton Salt Co.* v. *G. S. Suppiger Co.,* 314 U.S. 488, 491-92; *Ethyl Gasoline Corp.* v. *United States,* 309 U.S. 436, 455-59; *International Business Machines Corp.* v. *United States,* 298 U.S. 131, 140; *Carbice Corp. of America* v. *American Patents Corp.,* 283 U.S. 27, 31; *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.,* 243 U.S. 502, 510-11.

Also for this reason, this Court has been reluctant to uphold state-created or enforced rights which in any way impede "full and free competition in the use of ideas which are in reality a part of the public domain." *Lear, Inc.* v. *Adkins*, 395 U.S. 653, 670. This basic policy, traceable to the writings of Thomas Jefferson, *see Graham* v. *John Deere Co.*, 383 U.S. 1, 7-9,[25] has been endorsed consistently by this Court.

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[25] The basic philosophical premise underlying this policy position is that disclosed ideas are inherently free, that material and scientific progress will in general be maximized by the free and unfettered exchange of ideas, and that the exclusive right to use and exploit ideas is a gift from society which must be narrowly limited to the purpose of inducing persons "to bring forth new knowledge." *Graham* v. *John Deere Co.*, 383 U.S. 1, 9. As Thomas Jefferson so eloquently stated:

> If nature has made any one thing less susceptible than all others of exclusive property, it is the action of the thinking power called an idea, which an individual may exclusively possess as long as he keeps it to himself; but the moment it is divulged, it forces itself into the possession of every one, and the receiver cannot disposess himself of it. Its peculiar character, too, is that no one possesses the less, because every other possesses the whole of it. He who receives an idea from me, receives instruction himself without lessening mine; as he who lights his taper at mine, receives light without darkening me. That ideas should freely spread from one to another over the globe, for the moral and mutual instruction of man, and improvement of his condition, seems to have been peculiarly and benevolently designed by nature, when she made them, like fire, expansible over all space, without lessening their density in any point, and like the air in which we breathe, move, and have our physical being, incapable of confinement or exclusive appropriation. Inventions then cannot, in nature, be a subject of property. Society may give an exclusive right to the profits arising from them, as an encouragement to men to pursue ideas which may produce utility, but this may or may not be done, according to the will and convenience of the society, without claim or complaint from any body. VI Writings of Thomas Jefferson, at 180-81 (Washington ed.), quoted in *Graham* v. *John Deere Co.*, 383 U.S. at 8-9, n.2.

Forty years ago, in *Kellogg Co.* v. *National Biscuit Co.*, 305 U.S. 111, 122, the Court observed that "[s]haring in the goodwill of an article unprotected by patent or trade-mark is the exercise of a right possessed by all —and in the free exercise of which the consuming public is deeply interested."

More recently, in *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, and *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234, the Court, making explicit what it had implied in *Kellogg*, concluded that a state could not bar "free access to copy whatever the federal patent and copyright laws leave in the public domain." 376 U.S. at 237. This conclusion was rooted firmly in the Court's perception of the complex interplay between the patent laws and the broader national policy of promoting free competition wherever possible, for as the Court explained in *Sears* (376 U.S. at 230-31):

> . . . *[T]he patent system is one in which uniform federal standards are carefully used to promote invention while at the same time preserving free competition.* Obviously a State could not, consistently with the Supremacy Clause of the Constitution, extend the life of a patent beyond its expiration date or give a patent on an article which lacked the level of invention required for federal patents. To do either would run counter to the policy of Congress of granting patents only to true inventions, and then only for a limited time. Just as a State cannot encroach upon the federal patent laws directly, it cannot, under some other law, such as that forbidding unfair competition, give protection of a kind that clashes with the objectives of the federal patent laws. (Emphasis added; footnotes omitted.)

Five years after deciding *Sears* and *Compco*, the Court, in *Lear, Inc.* v. *Adkins*, 395 U.S. 653, reaffirmed its position that there is a "strong federal policy favor-

ing free competition in ideas which do not merit patent protection," *id.* at 656, and concluded, in a factual context similar to that in the present case,[26] that "the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain." *Id.* at 670. Consequently, the Court held that "federal law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent." *Id.* at 668.

[26] In *Lear*, Adkins, the inventor of an improved method of constructing gyroscopes, applied for a patent on the process in 1954, and in 1955 entered into a licensing agreement with Lear. In 1957, Lear refused to pay royalties, claiming that Adkins' gyroscope was fully anticipated in prior art and therefore was unpatentable. In 1960, Adkins' patent issued, Adkins sued to collect royalties for the entire patent period and Lear defended on the grounds of patent invalidity. This Court granted certiorari to reconsider the licensee estoppel doctrine "in the light of [its] recent decisions emphasizing the strong federal policy favoring free competition in ideas which do not merit patent protection." 395 U.S. at 656. After overturning the doctrine of licensee estoppel, the Court held that enforcing a contractual provision requiring the payment of royalties on the subject of an invalid patent "would undermine the strong federal policy favoring full and free use of ideas in the public domain" and therefore could not be given effect. 395 U.S. at 674.

Contrary to petitioner's contentions (*see* Br. 20-23), there is no distinction between the situation in *Lear*, where a patent application was licensed, a patent issued, and the patent was then declared invalid and the situation here, where a patent application was licensed, the Patent Office refused to issue a patent, and the patent application was abandoned. In both cases, the licensed items are in the public domain, *see Scott Paper Co.* v. *Marcalus Mfg. Co.*, 326 U.S. 249, 263 (Frankfurter, J., dissenting), *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 231, and therefore both may be produced by anyone who desires to do so. *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234, 237; *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 231.

Again, in *Goldstein* v. *California*, 412 U.S. 546, the Court explained that states could not be allowed to extend patent-type rights to holders of unpatented articles because such action would disturb the delicate balance Congress had drawn between the need to stimulate invention and the need to maximize competition. This Court said (412 U.S. at 569-70):

> In regard to mechanical configurations, Congress had balanced the need to encourage innovation and originality of invention against the need to insure competition in the sale of identical or substantially identical products. The standards established for granting federal patent protection to machines thus indicated not only which articles in this particular category Congress wished to protect, but which configurations it wished to remain free. The application of state law in these cases to prevent the copying of articles which did not meet the requirements for federal protection disturbed the careful balance which Congress had drawn and thereby necessarily gave way under the Supremacy Clause of the Constitution.

Finally, in *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, this Court, while holding that state trade secret law was not preempted by federal patent law, cited with approval its previous decisions in *Sears* and *Compco*, noting that trade secrets are by definition not in the public domain. 416 U.S. at 484. Thus, this Court in *Kewanee* reiterated its support for the basic proposition that ideas in the public domain must be available in free and full competition without any state-created or enforced impediment, though "ideas in the public domain" was defined so as to exclude trade secrets, since trade secrets by their very nature exist only when maintained in secrecy. *Id.; see* Oppenheim, *The Pa-*

tent-Antitrust Spectrum of Patent and Know-How License Limitations: Accommodation? Conflict? or Antitrust Supremacy?, 15 Idea 1, 20 (1971) ("[i]deas in general circulation are obviously in the public domain").[27]

Read together, the decisions of this Court establish that if an idea has been disclosed and is neither a trade secret nor patented, it is in the public domain. In this situation this Court has held that there is a strong federal policy to ensure free and full competition in the use of such ideas "lest in the constant demand for new appliances the heavy hand of tribute be laid on each slight technological advance in an art," *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 230, *quoting Cuno Engineering Corp.* v. *Automatic Devices Corp.*, 314 U.S. 84, and the finely-tuned balance between the patent system and the mandate for a competitive economy be undermined. *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 230-31. As is shown below, enforcement of the contract right to indeterminable payments claimed by petitioner would undercut these longstanding principles, and, in so doing, create anti-competitive influences inimical to our free market economy.

[27] This interpretation appears to comport with the position taken in a recent review of the subject undertaken by one Senate subcommittee. On February 5, 1976, the Senate Subcommittee on Patents, Trademarks and Copyrights of the Senate Judiciary Committee approved S. 2255, Section 301 of which dealt explicitly with patent law preemption. The Subcommittee explained (S. Rep. No. 642, 94th Cong., 1st Sess., 43 (1976)):

> This section [section 301] provides, first, that title 35, shall not be construed to preempt state law of trade secrets. The latter term will be defined by the courts.
>
> Subsection (b) states that the language of subsection (a) does not authorize "any state to grant any person the right to limit the full and free use by the public of ideas in the public domain or in general circulation." Nothing contained in either subsection of section 301 shall be interpreted as altering or qualifying in any respect the holdings of the Supreme Court in *Kewanee Oil Company* v. *Bicron Corporation; Lear, Inc.* v. *Adkins; Compco Corp.* v. *Day-Brite Lighting, Inc.*, and *Sears Roebuck & Co.* v. *Stiffel Co.*

The Senate passed the bill, but the House did not act on the legislation and S. 2255 died when Congress adjourned. The Subcommittee's explanation of Section 301, does, however, show some Congressional support for the view that true trade secret protection is not inconsistent with the general rule favoring free competition in the use of ideas in the public domain.

B. Petitioner's Keyholder Is an Idea in the Public Domain; Enforcing a Contractual Provision for Continuing Royalties on the Subject Matter of an Abandoned Patent Application Where the Subject Matter Is in General Circulation Undermines the Federal Policy in Favor of Free and Full Use of Ideas in the Public Domain and Conflicts With National Competition Policy.

Petitioner's keyholder, like the lighting fixtures in *Sears* and *Compco*, is an idea in the public domain. Like the lighting fixtures in *Sears* and *Compco*, petitioner's keyholder is unpatented. Like the lighting fixtures in *Sears* and *Compco*, petitioner's keyholder was fully and rightfully disclosed as soon as it was marketed. Like the lighting fixtures in *Sears* and *Compco*, petitioner's invention is now in general circulation, and competitors are freely producing the item. Unlike the secret industrial process this Court considered in *Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, petitioner's unpatented idea is not a trade secret. Rather, it is an idea in the public domain with respect to which there is to be free and full competition, unfettered by conflicting state law. *See Lear, Inc.* v. *Adkins*, 395 U.S. 653; *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225; *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234.

A state may seek to impede competition in the use of ideas in the public domain not only through direct means such as the enforcement of unfair competition laws, *see Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234, but also by enforcing contractual provisions contrary to the strong federal policy of encouraging open competition with respect to such ideas. *See Lear, Inc.* v. *Adkins*, 395 U.S. 653; *Brulotte* v. *Thys Co.*, 379 U.S. 29. As the Court explained in *Northern Pacific Railway Co.* v. *United States*, 356 U.S. 1, 4-5:

> The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competition forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. But even were that premise open to question, the policy unequivocally laid down by the Act is competition. And to this end it prohibits "Every contract, combination . . . or conspiracy, in restraint of trade or commerce among the several States."

Thus, a contractual provision requiring the continuing payment of royalties on an unpatented device in general circulation, no less than state unfair competition laws, may exert a cloistering effect on free markets, *see Lear, Inc.* v. *Adkins*, 395 U.S. 653, and such influences have no more place here than they did in *Brulotte* v. *Thys Co.*, 379 U.S. 29, 32-33.

Where state contract law conflicts with federal policies ensuring the availability of free markets for ideas such as petitioner's keyholder, state law must give way to federal policy, for otherwise "the public may continually be required to pay tribute to would-be monopolists without need or justification." *Lear, Inc.* v. *Adkins*, 395 U.S. 653, 670. Such tribute is what petitioner seeks to obtain in this case; such tribute, if allowed to be exacted will undermine the federal competitive mandate, just as this Court concluded it did in *Lear*.

Enforcing royalty payments for use of an invention during the period a patent application is pending may well be justified on both economic and equitable grounds because the licensor, by disclosing his invention to a licensee, will have provided that licensee an important headstart advantage for which the licensee should pay. *See Lear, Inc.* v. *Adkins*, 395 U.S. 653, 671-72, 682, n. 2 (White, J., concurring in part); Doerfer, *The Limits on Trade Secret Law Imposed by Federal Patent and Antitrust Supremacy*, 80 Harv. L. Rev. 1432, 1445, 1451-52 (1967).

However, just as pre-issuance and post-issuance patent royalties stand on a different footing, *see Lear, Inc.* v. *Adkins*, 395 U.S. 653, 682, n. 2 (White, J., concurring in part), so also do pre- and post-rejection royalties. After the patent application upon which the licensing agreement was predicated is denied, the second half of the licensee's bargained-for consideration—the right to exclusive use of the invention—disappears, because the licensor, having been refused a patent, will never have this exclusive right to convey. After this time, any royalties exacted for further use of the invention will be excessive because such royalties will include payment for exclusive use as well as for disclosure. The

licensor cannot convey the right to such exclusive use at this point, and the licensee no longer has any hope of obtaining the exclusive right for which it bargained.

The anti-competitive effects of requiring a licensee to continue paying excessive royalties long after his licensor has abandoned the application upon which the parties' licensing agreement was predicated are especially severe where, as here, the item which was the subject of the licensing agreement is being freely produced by the licensee's competitors. Coerced payment of such royalties for an item in general circulation adds to the cost of production and can, in certain circumstances, be the marginal increment to costs which makes production not economically viable. To the extent that competition is inhibited by requiring one producer to pay royalties, prices will tend to be higher for all producers and the ultimate burden falls on the public.

In this case, the excessive royalties paid by respondent add to its cost of producing the keyholder, making it increasingly difficult for it to compete in the keyholder market. Quick Point's share of the market has already declined and will probably continue to do so if it is forced to continue paying royalties on an item for which it is not receiving its bargained-for consideration (exclusive use) while its competitors remain free to produce petitioner's keyholder free of charge. The elimination of even one competitor may provide a basis for antitrust liability, *see Klor's, Inc.* v. *Broadway-Hale Stores, Inc.*, 359 U.S. 207, 213. Consequently, "[licensors] having the power to place licensees needing to compete in a potentially ruinous or uneconomic situation should not be condoned." Worthing, *Know-*

How Misuse: A Potential Weapon for Licensees, 53 J. Pat. Off. Soc'y 177, 187 (1971).[23]

Thus, while it may be justifiable to allow a licensor to collect royalties on an unpatented idea during the pendency of a patent application, enforcement of royalties long after a patent application has been abandoned and the subject is fully in the public domain would have the undesirable effect of funneling excessive rewards to the licensor at the expense of the licensee, for "[a] licensor's exacting royalties for sales or use of know-how after its period of commercial vitality has expired bears little relation to the licensor's investment in the know-how development or the expected return from its use." Worthing, *Know-How*

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[23] Recognition of the harmful anti-competitive effects which could result from requiring licensees to continue paying royalties after the licensed item has lost any secrecy it might once have had has prompted numerous leading legal scholars to favor cessation of royalty payments on non-patented items once the items have been disclosed and are in general circulation. *See, e.g.*, Adelman, *An Antitrust Decision: Lear* v. *Adkins*, 58 A.B.A.J. 45, 46 (1972); Worthing, *Know-How Misuse: A Potential Weapon for Licensees*, 53 J. Pat. Off. Soc'y 177, 190-93 (1971); Stern, *A Reexamination of Preemption of State Trade Secret Law After Kewanee*, 42 Geo. Wash. L. Rev. 927, 989 (1974). *See also Choisser Research Corp.* v. *Electronic Vision Corp.*, 173 U.S.P.Q. 234 (Cal. Super. Ct. 1972).

The same concern for protecting competition and minimizing the perpetuation of monopoly influences with respect to ideas is manifest in the practice in the lower courts of limiting injunctions, even in true trade secret cases, to a period measured by the "head-start" advantage which should be accorded the developer of a trade secret. *See, e.g., Winston Research Corp.* v. *Minnesota Mining and Manufacturing Co.*, 350 F.2d 134, 143 (9th Cir. 1965); *Conmar Products Corp.* v. *Universal Slide Fastener Co.*, 172 F.2d 150, 156 (2d Cir. 1949). *See generally* Comment, *The Viability of Trade Secret Protection After Lear* v. *Adkins*, 16 Vill. L. Rev. 551, 563-66 (1971).

Misuse: A Potential Weapon for Licensees, 53 J. Pat. Off. Soc'y 177, 191 (1971). Consequently, the licensee will be placed in an adverse position vis-à-vis his competitors and the very anti-competitive effects this Court has consistently attempted to prevent, *see* Goldstein, *The Competitive Mandate: From Sears to Lear,* 59 Calif. L. Rev. 873, 873-86 (1971), will be encouraged.

IV. THIS CONTRACT, WHICH, IF ENFORCED, WOULD REQUIRE QUICK POINT TO CONTINUE PAYING ROYALTIES INDEFINITELY ON THE SUBJECT MATTER OF AN ABANDONED PATENT APPLICATION CONFLICTS WITH BOTH NATIONAL COMPETITION POLICY IN GENERAL AND THE UNITED STATES PATENT LAWS IN PARTICULAR, AND IS THEREFORE PREEMPTED BY FEDERAL LAW AND POLICY.

The heart of the issue in this case, as it was in *Lear, Inc.* v. *Adkins,* is the accommodation of the competing demands of the common law of contracts and the federal law requiring "full and free competition in the use of ideas which are in reality a part of the public domain." 395 U.S. at 670. Where the two conflict, state law is preempted and must give way to overriding federal law and policy. *Lear, Inc.* v. *Adkins,* 395 U.S. 653, 673-74.

In this case, as in *Lear,* a contractual provision calling for continued payment of royalties on an item for which patent status was sought and later denied cannot be enforced, for to do so would: (1) conflict directly with the patent laws; (2) frustrate overriding federal policies designed to ensure "full and free competition in the use of ideas which are in reality a part of the public domain." *Lear, Inc.* v. *Adkins,* 395 U.S. 653, 670; (3) upset the economic balance between the promotion of invention and the preservation of free competition which Congress intended to strike in the pat-

ent laws, *see Sears, Roebuck & Co.* v. *Stiffel Co.,* 376 U.S. 225, 230; and (4) needlessly introduce harmful anti-competitive influences into the free marketplace of ideas.

"[I]t is 'familiar doctrine' that . . . federal policy 'may not be set at naught, or its benefits denied,' by . . . state law." *Kewanee Oil Co.* v. *Bicron Corp.,* 416 U.S. 470, 479-80, *quoting Sola Elec. Co.* v. *Jefferson Elec. Co.,* 317 U.S. 173, 176. Because petitioner's contract, if interpreted to require continuing royalty payments, conflicts directly with the patent laws in particular and national competition policy in general, it is unenforceable under federal law.

The position that petitioner's contract conflicts with, and must therefore yield to, federal law, is underscored by the fact that countervailing state policies and equitable considerations are so weak. This case, unlike *Kewanee Oil Corp.* v. *Bicron Corp.,* 416 U.S. 470, does not require this Court to set aside a body of longstanding state law designed to further legitimate and important state objectives such as the promotion of commercial morality. This case, unlike *Automobile Workers* v. *Russell,* 356 U.S. 634, and *United Construction Workers* v. *Laburnum Construction Corp.,* 347 U.S. 656, does not involve "conduct marked by violence or imminent threats to the public order" and a consequent "compelling state interest . . . in the maintenance of domestic peace." *San Diego Building Trades Council* v. *Garmon,* 359 U.S. 236, 247. This case, unlike *Lear, Inc.* v. *Adkins,* 395 U.S. 653, does not even involve an established rule of state contract law such as licensee estoppel, which this Court found preempted by federal patent law.

Non-enforcement of this contract would not be unjust to petitioner. Although an inventor has the option of

seeking patent or alternative state protection, he is not necessarily entitled to the cumulative benefits afforded by both systems. *See Kewanee Oil Co.* v. *Bicron Corp.*, 416 U.S. 470, 483; *United States* v. *Dubilier Condenser Corp.*, 289 U.S. 178, 186; *Pennock* v. *Dialogue*, 2 Peters 1, 18; *Troxel Manufacturing Co.* v. *Schwinn Bicycle Co.*, 465 F.2d 1253, 1258 (6th Cir. 1972); *Painton & Co.* v. *Bourns, Inc.*, 442 F.2d 216, 224-25 (2d Cir. 1971); *Metallizing Engineering Co.* v. *Kenyon Bearing & Auto Parts Co.*, 153 F.2d 516, 520 (2d Cir. 1946), *cert. denied*, 328 U.S. 840.

Although it may be equitable to allow an inventor to collect royalties *during* the time his patent application is pending, it is an entirely different matter to require a licensee to continue paying royalties *indefinitely after* the application upon which the licensing agreement was based has been abandoned. Only royalty payments of the latter type are at issue in this case, and these payments, because they conflict with both the patent laws and general pro-competition policy objectives consistently endorsed by this Court, are preempted by overriding federal law and policy.

V. THE CONTRACT SHOULD NOT BE CONSTRUED TO REQUIRE CONTINUING ROYALTY PAYMENTS: SINCE BOTH PARTIES ENTERED INTO THE CONTRACT ASSUMING A PATENT WOULD ISSUE, AND SINCE THIS INTENT WAS FRUSTRATED BY PETITIONER'S FAILURE TO OBTAIN A PATENT, QUICK POINT IS DISCHARGED FROM ANY FURTHER DUTY TO CONTINUE PAYING ROYALTIES TO PETITIONER.

The cardinal rule for construing a contract is to ascertain and give effect to the intent of the parties. *Kansas City, Missouri* v. *Kansas City, Kansas*, 393 F. Supp. 1, 4-5 (W.D. Mo. 1975). In this case, the intent shared by both parties, which became the cornerstone of their

contract, was that a patent would issue on petitioner's keyholder. Because no patent ever issued on petitioner's keyholder, respondent's duty to continue making royalty payments is discharged. *See Drackett Chemical Co.* v. *Chamberlain Co.*, 63 F.2d 853 (6th Cir. 1933).

The language of the licensing contract clearly manifests both parties' expectation that a patent on petitioner's keyholder would issue, and that the issuance of this patent was a basic assumption underlying their formation of the contract. In the main body of the agreement, petitioner explicitly promised respondent the "exclusive right" to manufacture and sell the keyholder on which her patent application was pending and agreed that in the event of "infringement" both parties would agree on what action would be taken. (App. 23-24.) As shown *supra* at 21, petitioner could convey the "exclusive right" she promised Quick Point only if she had succeeded in patenting her keyholder. Similarly, "infringement" would become an issue only if petitioner had succeeded in obtaining the patent both parties expected to be granted. *See* 35 U.S.C. § 271(a) (1970). Obviously, both parties expected a patent to issue on petitioner's keyholder because any other intent would render meaningless the clauses concerning exclusivity and infringement.

Petitioner, however, completely ignores the exclusivity and infringement language used in the main body of the agreement with Quick Point and contends that an addendum to the contract guarantees her continuing royalties on the keyholder. This addendum, which was

written by the petitioner as an addition to the contract (and not substituted for it, App. 25), states that:

> In the event that the Keyholder Patent Application Number 542677 is not allowed within five (5) years, Quick Point Pencil Co. agrees to pay Jane Leopoldi two and one-half percent ($2\frac{1}{2}\%$) of sales at selling prices, as long as you continue to sell same. (App. 25.)

Petitioner, focusing solely on the last clause of this addendum (*i.e.*, "as long as you continue to sell same") argues that this addendum obligates Quick Point to continue paying royalties as long as it continues to manufacture petitioner's keyholder regardless of whether a patent on the keyholder ever issued. (Br. 25, 27.)

This interpretation does violence to both the language of the addendum and to basic contract doctrine. The addendum does not state that even if petitioner never obtained a patent on its keyholder, Quick Point would still be obligated to pay royalties indefinitely on its manufacture and sale of the keyholder; it states only that if a patent were not obtained *within five years* Quick Point's royalties would be reduced to $2\frac{1}{2}\%$. The addendum assumes that a patent would eventually issue but merely provides for the possibility that the patent would issue at a date more than five years after the date of the license.[29] Contrary to the assumption of amicus United States, the triggering event for reduction of royalties was not the denial of

[29] This was a realistic possibility for the decision of the Board of Patent Appeals denying petitioner's patent application was not made until more than five years after the date of the license. (App. 54.)

a patent *per se* (Br. 14), but rather the failure to obtain a patent *within five years*. The agreement did not require, as the United States contends (Br. 2), that the respondent pay a specified royalty if a patent were granted or, in the alternative, a reduced royalty if no patent were granted. If a patent had been obtained in the sixth year after the parties had signed their agreement, the royalties still would have been reduced to $2\frac{1}{2}\%$. Both parties assumed that a patent would issue; the only question was when.

If petitioner intended Quick Point's obligation to pay royalties to continue without regard to the issuance of a patent *at any time*, she, as drafter of the addendum, was obligated to state this expressly and unambiguously. *See, e.g., Floater Vehicle, Inc.* v. *Tryco Manufacturing Co.*, 497 F.2d 1355, 1358 (C.C.P.A. 1974); *Pipkin* v. *FMC Corp.*, 427 F.2d 353, 357 (5th Cir. 1970); *April Productions, Inc.* v. *G. Schirmer, Inc.*, 308 N.Y. 366, 372, 126 N.E.2d 283, 289 (N.Y. Ct. App. 1955). *See generally* Williston on Contracts § 621, at 760-62 (1961). Instead, petitioner now urges upon this Court an interpretation of her addendum which conflicts directly with the main body of the agreement which she explicitly accepted. In so doing, petitioner ignores settled contract doctrine which requires that different parts of a contract be read in conjunction with one another, that the intent of the parties be gleaned from the entire contract, and that different parts of the contract be harmonized wherever possible. *See, e.g., City of Harlan* v. *Duncan Parking Meter Corp.*, 231 F.2d 840, 841-42 (8th Cir. 1956). *See generally* Williston on Contracts § 618, at 710-11 (1961).

The rule of contract law applicable to this situation is that petitioner's failure to obtain the patent which

formed the explicit basis of their agreement discharges its obligation to continue paying royalties under the contract for, as explained in the Restatement of Contracts § 288 (1932) at 426:

> Where the assumed possibility of a desired object or effect to be attained by either party to a contract forms the basis on which both parties enter into it, and this object or effect is or surely will be frustrated, a promisor who is without fault in causing the frustration, and who is harmed thereby, is discharged from the duty of performing his promise unless a contrary intention appears.[30]

In this case, the parties' licensing agreement explicitly refers to petitioner's patent application, and the assumed acquisition of patent rights by petitioner formed the basis of the parties' agreement. This object was frustrated when petitioner abandoned her patent application seventeen years ago because, as petitioner readily admits, exclusivity may be obtained only under the patent laws (Br. 19), and Quick Point, therefore, never obtained the exclusivity for which it had bargained. (Br. 7, 20.) Quick Point was harmed by the rejection and abandonment of petitioner's application because it thereby lost its "exclusive right" to manufacture and sell petitioner's keyholder. Thus, Quick Point is discharged from having to make further royalty payments under its contract with petitioner.[31]

[30] The best known example of this "frustration of purpose" doctrine is the "Coronation case," *Krell* v. *Henry*, [1903] 2 K.B. 740 (Ct. App.). There the defendant had agreed to rent a flat in London for two stated days on which the coronation processions of Edward VII were scheduled. Due to the illness of the King, the processions did not take place on the days originally scheduled, and the defendant declined to pay the balance of the rent for which he had contracted. The court, finding that the occurrence of the procession was the "foundation" of the contract, held that defendant would be discharged from further obligation to pay under its contract even though the contract was specific as to the dates, and contained no express reference to the coronation procession or to any other purpose to be served by the agreement.

CONCLUSION

For all the foregoing reasons, the judgment of the Eighth Circuit Court of Appeals should be affirmed.

Respectfully submitted,

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[31] This result is further supported by the understandable reluctance of the courts to construe contracts so as to require performance for an indefinite time. Promises of performance without a definite time limit should be interpreted to require performance for only a "reasonable" time, *see Freeport Sulphur Co.* v. *Aetna Life Ins. Co.*, 206 F.2d 5, 8 (5th Cir. 1953), 3A Corbin on Contracts § 684, at 231 (1960), for "[p]erpetual contracts, though sometimes sanctioned, are not favored in the law. A construction of a contract conferring a right in perpetuity will be avoided unless compelled by the unequivocal language of the contract." 206 F.2d at 8.

Quick Point has already paid royalties for nineteen years even though it lost all hope of ever obtaining the "exclusive right" to manufacture and sell petitioner's product in 1961 when petitioner abandoned her patent application. Clearly, a "reasonable" time for the payment of royalties has already passed, and construction of the licensing contract to require that respondent continue paying royalties indefinitely despite the fact that it will never obtain the "exclusive right" for which it bargained is neither "compelled by the unequivocal language of the contract," nor justified under standard contract construction doctrines.